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THE ASSOCIATION FOR UK INTERACTIVE ENTERTAINMENT

halo financial

Currency Management

If you expand into overseas markets, something you will have to address will be the currency exchange aspects of your international business. That may sound like a whole heap of hassle you would rather do without but it really doesn't have to be that way.

Well managed foreign exchange risk can actually be an opportunity and not just an irritation. And on the flip side of that, poorly managed foreign exchange risk tends to be expensive. So where do you start?

Cash management

There are advantages to holding bank accounts in the relevant currencies. It affords you a great deal of flexibility in holding currencies, timing conversions and managing transfer costs. Most currencies can be held in accounts in the UK but you may find it is cheaper and easier to hold accounts in the relevant countries. Some bank portals allow control of overseas accounts through an online solution. It is worth checking facilities with your own bank.

If you do so, check whether there are any receiving fees for inbound transfers. Some banks, especially Spanish banks, charge a percentage of the transferred amount and that can run into thousands of pounds in extra costs. You can usually avoid this if you pay tranches of less than €50,000 at a time but you can negotiate with the Spanish bank to agree a fixed cost in advance.

It is best to refuse to accept currency cheques or drafts for payment unless you have a bank account in the country the cheques are drawn on. The costs are prohibitive and the delay in receiving clear funds can take 6-8 weeks.

Transfers

If you need to make Euro payments anywhere within Europe, use SEPA transfers whenever possible. These offer much lower costs than traditional wire transfers and are just as speedy. For everywhere else, international SWIFT transfers are the tool for the job and most banks and brokers offer this format.

Buying and selling

It is always worth thinking well in advance on exchange rates. Some companies cover all their risk the minute it is apparent and others wait until the last possible minute before even booking an exchange rate. Both choices have their advantages and pitfalls.

Monthly fluctuations of 5% or more are the norm and that can be very costly or hugely frustrating if you miss the better rate for the sake of a bit of basic forward planning. That planning doesn't need to be any more than a spreadsheet showing requirements and a strategy to cover the risk. However, Murphy's Law dictates that last minute booking is rarely a good option.

Use the markets own tools for best currency management. That might include booking forward contracts to fix an exchange rate today for settlement up to 2 years ahead or placing automated orders to guarantee a 'worse case' exchange rate whilst leaving room to take advantage of positive exchange rate movement.

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How much do fluctuating exchange rates affect my money transfers?

Example 1
UK importer from Europe receives an invoice for €250,000 on 1st August 2013. The invoice is due for payment on 60 day terms. If the importer bought all the euros on 1st August, the exchange rate would have been €1.14 to the Pound. That equates to a Sterling cost of £219,298. 60 days later, as at 1st October, the settlement date for the invoice, the exchange rate reached a high of €1.20; a 5.2% saving. The importer could have saved nearly £11,000 on the contract through little more than good timing and access to currency market expertise.

Example 2
On 1st August 2013, a UK based exporter invoiced a US customer for $200,000. They are due to receive the funds in 90 days. The exporter called his Halo Financial Consultant and discussed the likely direction of the Sterling – US Dollar exchange rate. As the trend was moving the exchange rate in the wrong direction for the exporter's needs, the decision was reached to sell the US Dollars on a forward contract at $1.52 to the Pound. As at 1st November, when the payment was received from the customer, the prevailing exchange rate was $1.60. Through good risk management and a fairly simple hedging tactic, the exporter saved £6,578 on the contract.

Example 3
A company in the UK has borrowed £3 million in a loan from a Japanese parent company. The exchange rate for the loan is set at Y120 to the Pound in January 2012. The loan is to be repaid in three £1 million tranches on the anniversary of the loan date. The subsidiary company has three main options. (A) Do nothing and hope the exchange rate doesn't worsen over the three year period. (B) Purchase the whole of the requirement on forward contracts to guarantee the exchange rate and ensure the loan value doesn't increase no matter what happens to the Sterling – Yen exchange rate. (C) Manage the risk of deterioration in the exchange rate through stop loss orders and take advantage of advantageous moves through forward contracts as and when those opportunities present themselves. As at January 2013, the GBP-JPY exchange rate was Y140 to the Pound and as at November 2013, the rate had climbed to Y160. Delaying the purchase of the 1st tranche could have equated to £142,000 of savings on £1 million worth. If the other £2 million was covered at Y160, the total saving on the loan would have been £642,000.

Rest assured

Whether you have a blanket policy on foreign exchange, adopt a more ad hoc approach or just wing it, the management of your foreign exchange needs will impact P&L. That might be a positive impact or a negative one but the impact will be felt. If you don't want the figure to have brackets around it when your accountant is done, it is always worthwhile setting your policy out in advance, being prepared to change and enlisting some expertise to manage things with you.

Without a plan, your profit is all riding on a gamble and that is no way to run a business. As a starting point, speaking with Halo Financial will help you determine what will work best for your business. But wherever you are in the business growth cycle, with a review of your existing arrangements, the right partner, and good timing, there is every opportunity to add value to the process of currency exchange and reduce or remove the risk associated with cross border transactions.

What should I do next?

For further information on this document contact David Johnson, at Halo Financial on 020 7350 5470 or visit halofinancial.com/ukie